Managing Compliance with SSARS 21

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CPAs serving the small- and medium-sized market must strike the right balance between complying with professional and regulatory standards, providing value-added client service, and mitigating litigation and other practice management risks. The purpose of this article is to identify best practices under Standards for Accounting and Review Services No. 21 (SSARS 21). Many CPAs will find ambiguous language removed from the standard, providing an opportunity to prepare financial statements without the burden of submitting a compilation report.

The significance of this SSARS may reveal itself as an unexpected surprise during the peer review process. Peer review helps to monitor a CPA firm's accounting and auditing practice. The goal of the program is to promote quality in the accounting and auditing services provided by American Institute of CPAs (AICPA) members and their CPA firms. This goal serves the public interest. There are two types of peer reviews: System Reviews and Engagement Reviews. System Reviews focus on a firm's system of quality control and Engagement Reviews focus on work performed on selected engagements. Whether subject to a system or an engagement review, a sample of SSARS 21 engagements is likely to be subject to review, and understanding and implementing the standard is essential when undergoing a peer review.

An important layer to the peer review complexity for CPAs is the increased focus on auditor independence. This issue has been especially challenging for accountants with clients who have trouble preparing financial statements in accordance with standards, creating a lingering question facing the profession: How does a CPA maintain independence when helping a client prepare financial statements?

In 2014, AICPA addressed the issue with its SSARS 21. The standards went into effect at the end of 2015. SSARS 21 provides a bright line between accounting services (preparation) and reporting services (compilation or review). The accountant no longer has to be concerned about whether a financial statement will be used only by management or by third parties. Its four sections allow a practitioner to evaluate the nature of the client relationship and select the best value-added service. CPAs are better positioned to focus on the unique needs of clients rather than deploying creative strategies to support the appearance of independence.

A Brief History of Compilation and Review Engagements

The 1971 landmark 1136 Tenants' Corporation case paved the way for compilation and review engagements. The case resulted in a sizeable judgment against a CPA firm sued by a cooperative apartment group for failing to uncover embezzlement.

The firm was hired to perform write-up services by the managing agent who committed the fraud. The financial statements clearly stated: "No independent verifications were undertaken," but the firm was found liable for failing to inquire about missing invoices. Without an audit engagement letter, the firm was unable to convince the court that the firm was not engaged to audit the financial statements.

Prior to 1978, accountants engaged to report on financial statements had two options: either perform an audit or issue a disclaimer of opinion on the financial statements. CPAs were required to evaluate financial statements from a perspective that the audit could be seen by third parties. With the issuance of SSARS No. 1, Compilation and Review of Financial Statements, in 1978, accountants were given another reporting option to address professional liability exposure associated with plain paper financial statements.

The basic standard for accountants who prepared and presented financial statements to their clients or to third parties was issued under Paragraph 7, stating "the accountant should not submit unaudited financial statements of a nonpublic entity to his/her client or others unless, as a minimum, he/she complies with the provisions of this statement applicable to a compilation engagement." The SSARS defined "submission" as "presenting to management financial statements that the accountant has prepared." As a result, accountants in public practice were required to perform a compilation engagement on those financial statements.

Submission was the equivalent of a compilation service when SSARS No.1 was issued, since paper statements were prepared and bound before presentation to clients. In today's electronic environment, financial data is often recorded in multiple computer platforms, including some in the "cloud." Computer software used by the client and the CPA makes it difficult to determine who prepared the statements.

Consider a situation where an accountant performs bookkeeping services. The CPA often has access to the client's cloud-computing system and may make a number of journal entries to record payroll

Table 1

SSARS Sections	Section 60 of SSARS 21	Section 70 of SSARS 21	Section 80 of SSARS 21	Section 90 of SSARS 21
When does the standard apply?	General principles for accounting and review services	Engagement to prepare financial statements	Engagement to perform a compilation	Engagement to perform a review
Purpose	Help CPAs understand professional responsibilities	Engagement to prepare financial statements without reporting on the statements	Engagement to perform a compilation engagement	Engagement to perform a review engagement
Major change?	No	Yes – Relevant for accountants who perform interim statements, use cloud computing and statements not expected to be used by third parties	No	No
Engagement letter required?	N/A	Yes	Yes	Yes
Independence required?	N/A	No	Yes	Yes
Report required	N/A	No	Yes	Yes

tax payments, sales tax payments, depreciation expense and revenue adjustments for a given period. The internal bookkeeper may account for recurring expenses and billing. The bookkeeper prints from the cloud accounting software for presentation to the owner. Who has prepared the financial statements – the accountant, the bookkeeper or the application?

Based on the original definition of submission, which focused on preparing and presenting, things worked well until technological advances muddied the waters. If the client sends a Quickbook file to a CPA and he/she makes adjustments to the financials, the work could impair independence.

The profession lived with the risk of potentially compromising independence. CPAs often discussed this issue during the peer review process and many firms were aware of the significant independence risk. Strategies included CPAs affiliating themselves with accounting service providers who would help clients prepare for an attest engagement. Many accountants were reluctant to relinquish services due to concerns about reduced billings and inserting another financial advisor into the equation. Clever CPA firms protected their independence by avoiding sending financial statements. They returned Quickbook files with recommended journal entries or created updated trial balance forms.

SSARS 21 eliminates the need for the CPA to answer the question of who prepared the financial statement. It eliminates the submission requirement. Table 1 includes key features that can help navigate the standards.

Section 60: General Principles for Engagements Performed in Accordance with Statements on Standards for Accounting and Review Services – This section provides general principles for engagements performed in accordance with SSARS. It identifies professional responsibilities when performing an engagement. An accountant used to perform a review, a compilation or an engagement to prepare financial statements is required to adhere to overall standards, as well as the appropriate engagement section. Section 60 provides guidance on:

- Ethical requirements
- Professional judgement
- Conduct of the engagement in accordance with SSARS
- Engagement-level quality control
- Acceptance and continuation of client relationships and engagements
- Conduct of the engagement in accordance with SSARS

Section 60 also requires accountants to agree upon the terms for all SSARS engagements with management or those charged with governance. The terms should be documented in an engagement letter with signatures of the accountant and those charged with governance to ensure management understands the arrangement.

Section 70: Preparation of Financial Statements – Section 70 is intended to be short and easy to apply for accountants engaged to prepare financial statements for clients without reporting on the statements. This section is especially helpful for those who prepare interim financial statements and perform cloud-based accounting services. This section can help accountants who prepare financial statements not expected to be used by a third party (management-use-only financial statements). Since this is a non-attest service, independence does not need to be determined.

Section 70 applies when an accountant in public practice is engaged to prepare financial statements. It does not apply when the accountant is engaged to perform an audit, review or compilation of those financial statements prepared by the accountant. If an accountant is engaged in an attestation service, it is important to recognize that assisting in the preparation of financial statements is a nonattest service (per ethics interpretation No. 101-3). The same applies when the accountant prepares financial statements as a byproduct of submission to taxing authorities, for personal financial plans, in conjunction with litigation or related to business valuation services.

In adopting the standard, SSARS 21 also embraces a principle-based approach, requiring accountants to apply professional judgment in determining if financial statements were actually prepared. Accountants should have conversations with clients to determine if the financial statements are part of the engagement for internal or external use. Because preparing financial statements is a nonattest service, there is no requirement to determine independence.

If the accountant prepares financial statements that omit substantially all disclosures required by the reporting framework, he/she is required to disclose the omission either in the statements or in a note to the statements. The accountant may also prepare financial statements that include limited disclosures and these disclosures should be labeled, "Selected Information – Substantially All Disclosures Required by the (reporting framework) Are Not Included." No accountant should omit disclosures if the intent is to mislead users of the statements. Finally, the accountant is required to include a statement on each page indicating, at a minimum, that "no assurance is provided" on the financial statements.

Section 80: Compilation Engagements – Section 80 applies when an accountant is used to perform a compilation engagement. This section differs from the prior compilations, which apply when the accountant

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prepared and presented financial statements to clients or third parties.

The objective in a compilation engagement is to apply accounting and financial reporting expertise to assist management in the presentation of the financial statements without providing any assurance about material modifications. Section 80 retains the independence requirement. The accountant can omit substantially all disclosures on financial statements.

A major change is the literature related to reporting on financial statements. A report is required. The old non-reporting exception that the statements would not be used by third parties is replaced with Section 70. Section 80 also streamlines compilations to highlight that no assurance is provided. The standard report is simply one paragraph without headings. Additional paragraphs may be required based on the reporting framework when management elects to omit disclosures, when independence is impaired, when a departure from the reporting framework is known or if supplemental information accompanies the statements.

Section 80 is significant, because accountants are relieved from the responsibility to determine if they "prepared and presented" the financial statement to clients.

Section 90: Review Engagements – Section 90 of SSARS No. 21 redrafts the existing literature with a few changes. This section clarifies the requirements and guidance for review engagements and redrafts the review literature in SSARS 19, including providing a review report that includes headings. It also contains a requirement to list the city and state of the issuing office with letterhead references acceptable to meet the disclosure.

Specific Practice Considerations

SSARS 21 provides more options for CPAs who participate in creating financial statements. Accountants need to assess their level of service to ensure compliance with the SSARS sections and communicate with clients to avoid liability exposure. The navigation required can be summarized in the areas of practice: engagement letters, pitfalls related to Section 70, the need to educate clients and peer review considerations.

Engagement Letters

SSARS demands that CPAs focus on engagement letters. It makes clear that CPAs must have a written understanding when reporting on or preparing financial statements. But the standard doesn't require the documentation when only engaged to perform bookkeeping or assisting with the preparation of financial statements. The best defensive documentation in situations not subject to the SAS or SSARS is to specifically describe services that will not be performed with engagement letter statements including the language, "we will not audit, review or compile or prepare financial statements."

SSARS 21 distinguishes between accountants preparing financial statements or those merely assisting with statements. If engaged to prepare financial statements, the accountant is subject to SSARS 21. Merely assisting with the preparation of financial statements is a bookkeeping function not subject to the standard. With an engagement letter clearly indicating that the services do not include the audit, review, compilation or preparation of financial statements, clients can't allege that the accountant was to have reported or prepared statements.

Additional engagement letter considerations include the need for the accountant to agree upon the terms for all SSARSs engagements with management or those charged with governance. CPAs should sign engagement letters prior to any work being performed and engagement letters should be obtained annually. An important consideration is to clarify the specified reporting framework, such as accounting principles generally accepted in the United States.

Section Considerations

Section 70 preparation of financial statements is a nonattest service. When accountants perform such engagements, they are not usually considering audits or reviews for the same year. If audit or review services are on the horizon, Section 70 engagement letters should spell out the client's responsibility to designate who is responsible for bookkeeping or preparation of financial statements.

Section 70 may still be confusing to some CPAs and their clients. The guidance offered in SSARS 21 fails to implicitly state that the CPA is providing "no assurance," the not-so obvious intent of the standard. The examples suggest that the client provides "no assurance." CPAs engaged to perform a preparation engagement should make clear in their engagement letters and each page of the financial statements that "No CPA provides any assurance on these financial statements."

Section 70 also states that the CPA's name is not required on the statements. Some CPAs think adding their name has marketing benefits, but it may only create additional litigation exposure. Don't offer to associate your name with any Section 70 prepared financial statement unless there is a compelling reason to do so.

Section 70 lists four exceptions to compliance when preparing financial statements and not engaged to perform an audit, review or compilation of the financial statements. The exceptions occur when the financial statements are included in personal financial plans, in conjunction with litigation services, in conjunction with business valuation and solely for submission to taxing authorities. When preparing tax returns, CPAs should not think they are working outside the boundaries of Section 70. It simply means federal tax returns don't count as financial statements subject to Section 70.

Section 80 conditions are expected to result in fewer compilation engagements due to the introduction of preparation services. Compilation literature applies when the accountant is engaged to perform compilation services. Section 80 mandates that reports accompany all financial statements, so management-use-only (formally SSARS 8) financial statements are no longer permitted. Also, the compilation report is distinguished from audits and reviews by using a one-paragraph report with no headings. Additional paragraphs are required when:

- Financial statements are prepared in accordance with a special purpose framework.
- Management elects to omit substantially all required disclosures.
- The CPA's independence is impaired.
- The financial statements have a known departure from the applicable reporting framework.

Educate Clients and Users of Financial Statements

Accountants should have thorough discussions with clients to make sure they understand the service to be performed, whether it will include a report and whether there will be a statement regarding "no assurance" on each page.

CPAs should recognize that clients and their bankers may wish to have a report accompany the financial statements. CPAs and clients should discuss the Section 70 Preparation Engagement service and contrast it with a compilation. Education is the key to having users make informed decisions and to avoid CPAs performing services that don't meet expectations or needs.

Additional opportunities for education include the need to explain the client's responsibility for judgments in financial statements. Clients may request assistance with significant judgments regarding amounts or disclosures. CPAs can use their expertise in helping with those determinations.

CPAs should also follow up on unusual findings regardless of the level of service. The Tenants case is a good example. CPAs should recognize risk factors. They may find client records are unsatisfactory and should bring the matter to the attention of management and ask for more appropriate information, even without the requirement for inquiries as part of an engagement.

Peer Review Considerations

Peer review results plunge and deficiencies increase dramatically when any new SSARS is put into effect. The same may occur with SSARS 21. Those subject to peer review when their highest level of service is preparation engagement can opt out of peer review.

Accountants should plan and perform the engagement to be consistent with current standards, paying close attention to proper planning, independence considerations, risk assessment, fraud considerations, firm administration and quality control.

The SSARS standards offer opportunities for CPAs to maintain independence while helping clients prepare financial statements. As most CPAs know, independence has grown in significance from a peer review perspective. Becoming familiar with SSARS 21 is a worthwhile endeavor for CPAs who help clients prepare financial statements, but need to maintain their independence. ■

The author wishes to acknowledge the following resources:

1. SSARS No. 21 Risk Management and Implantation Issues. Duncan B. Will. CAMICO. Aug. 11, 2015.
2. Statements on Standards for Accounting and Review Services: Clarification and Recodification. Issued by the Accounting and Review Services Committee of AICPA.
3. A bright line in SSARSs. *Journal of Accountancy*. Michael L. Brand, Michael P. Glynn and Charles McElroy. Dec. 1, 2014.
4. SSARS 21 and its impact on your firm. Jerome R. Reutzel. *Footnote Magazine*. December 2015.
5. Engagements to prepare financial statements. Implementation guidance for a transition from SSARS 19 to SSARS 21. *Footnote Magazine*. Barbara Beltrand

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